Office-Supreme Court, U.S.
FILED
MAR 22 1983
ALEXANDER L. STEVAS,
CLERK

No. 82-1270

In the Supreme Court of the United States

OCTOBER TERM, 1982

LOMAS SANTE FE, INC., ET AL., PETITIONERS

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

MEMORANDUM FOR THE RESPONDENT IN OPPOSITION

REX E. LEE
Solicitor General
Department of Justice
Washington, D. C. 20530
(202) 633-2217

TABLE OF AUTHORITIES

Page

Cases:

Bell v. *Harrison*, 212 F.2d 253 3

C.G. Sloan & Co. v. *Commissioner*, 38 T.C. 203 3-4

Century Electric Co. v. *Commissioner*, 15 T.C. 581, aff'd, 192 F.2d 155, cert. denied, 342 U.S. 954 ..... 4, 5

Commissioner v. *Moore*, 207 F.2d 265 3

Edinboro Co. v. *United States*, 224 F. Supp. 301 3

Fry v. *Commissioner*, 31 T.C. 522, aff'd, 283 F.2d 869 3

Gist v. *United States*, 423 U.S. 118 3

Home Trust Co. v. *Commissioner*, 65 F.2d 532 3

Miller v. *Commissioner*, 68 T.C. 767 5

1220 Realty Co. v. *Commissioner*, 322 F.2d 495 3

United States v. *Georgia R.R. & Banking*, 348 F.2d 278, cert. denied, 382 U.S. 973 ..... 3, 4

Statute and regulation:

Internal Revenue Code of 1954, 26 U.S.C. 1503(a) 1

Treasury Regulations on Income Tax (1954 Code), 26 C.F.R. 1.1502 2

In the Supreme Court of the United States

OCTOBER TERM, 1982

No. 82-1270

LOMAS SANTE FE, INC., ET AL., PETITIONERS

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

MEMORANDUM FOR THE RESPONDENT IN OPPOSITION

In this federal income tax case, petitioners[1] seek review of the decision below holding that they were not entitled to a deduction for depreciation claimed with respect to a 40-year estate for years reserved in a golf course.

---

[1]Lomas Sante Fe Country Club and Norco Landscape & Maintenance Co. are subsidiaries of Lomas Sante Fe, Inc. The three corporations are jointly liable for any deficiency in their tax for their tax year ending July 31, 1973, because they filed a consolidated corporate income tax return. Section 1503(a) of the Internal Revenue Code of 1954 (26 U.S.C.); Treasury Regulations on Income Tax (1954 Code), 26 C.F.R. 1.1502-2. Lomas Sante Fe, Inc. and Lomas Sante Fe Country Club are referred to as "Lomas" and "Country Club", respectively. Norco Landscape & Maintenance Co. is a party only because of its joint liability for the deficiency (Pet. App. B-2).

The pertinent facts may be summarized as follows: In 1964, Lomas began development of a high quality residential community which was to include country club facilities. On November 14, 1968, Country Club was organized to administer the country club facilities, and to hold title to the various properties used in the club's operations. On February 11, 1969, Lomas transferred the club facilities to Country Club, subject to the reservation of a 40-year estate in the golf course, golf professional shop, existing clubhouse, and an area planned for a future clubhouse, in exchange for all of the outstanding shares of Country Club. Lomas calculated its basis for tax purposes ($855,086) in the estate for 40 years in the golf course and its landscaping by applying an actuarial valuation factor of .7474275 to the costs of those assets ($1,151,244) (Pet. App. A-3, B-3 to B-10).

On their consolidated return for the taxable year ending July 31, 1973, petitioners claimed a depreciation deduction of $21,377.16 for amortization of the portion of the estate for 40 years which represented Lomas' interest in the land and landscaping making up the golf course. In addition, petitioners modified the computation of their net operating loss carryover to the taxable year ended July 31, 1973, by including an "amortization correction" in the amount of $21,377.16 for the taxable year ended July 31, 1972. In determining a deficiency in petitioners' federal corporate income tax for the taxable year ended July 31, 1973, the Commissioner disallowed the depreciation deduction taken in respect of the estate for 40 years in the golf course, and eliminated the "amortization correction" from their computation of the operating loss carryover (Pet. App. A-3, B-8 to B-12).

In the tax court proceeding brought by petitioners to redetermine the deficiencies, the tax court upheld the Commisioner's ruling that the golf course properties, prior to the transfer of the remainder interest to Country Club,

were nondepreciable due to their indefinite useful life, and could not become depreciable by transferring a remainder interest to a wholly owned subsidiary. In so holding, the tax court relied on *United States* v. *Georgia R.R. & Banking*, 348 F.2d 278 (5th Cir. 1965), cert. denied, 382 U.S. 973 (1966), which ruled that the taxpayer could not create a depreciable interest in otherwise nondepreciable stock of other corporations by distributing a remainder interest to its shareholders as a dividend and retaining an estate for 26 years in the stock (Pet. App. A-3 to A-4, B-27 to B-33). The court of appeals affirmed, with one judge dissenting (Pet. App. A-1 to A-7).

1. The decision below correctly held that petitioners were not entitled to a depreciation deduction with respect to the estate for 40 years in the golf course. It is clear that the real property comprising a golf course (*i.e.*, land, contouring and landscaping) has an indeterminate useful life, and is not depreciable for tax purposes. See *Edinboro Co.* v. *United States*, 224 F. Supp. 301 (W.D. Pa. 1963); see also *Commissioner* v. *Moore*, 207 F.2d 265, 268-269 (9th Cir. 1953). To be sure, a terminable interest in property having an indefinite useful life may itself be depreciable, if the interest is acquired by an investment separate from that with which the remainder interest is acquired. *Gist* v. *United States*, 423 F.2d 1118 (9th Cir. 1970); *Bell* v. *Harrison*, 212 F.2d 253, 255 (7th Cir. 1954); *1220 Realty Co.* v. *Commissioner*, 322 F.2d 495 (6th Cir.1963); *Home Trust Co.* v. *Commissioner*, 65 F.2d 532 (8th Cir. 1933); *Fry* v. *Commissioner*, 31 T.C. 522 (1958), aff'd, 283 F.2d 869 (6th Cir.1960). But as the courts below correctly held, a taxpayer cannot create a depreciable interest in property having an indefinite useful life by purchasing the fee simple interest and then dividing his rights by a tax-free transfer of the remainder interest to a wholly owned corporation. See *United States* v. *Georgia R.R. & Banking*, *supra*, 348 F.2d at 287-289; *C.G. Sloan & Co.* v. *Commissioner*, 38 T.C.

203, 211 (1962). Lomas obviously did not acquire a depreciable interest in the golf course by dividing its rights between an estate for 40 years and a remainder and transferring the remainder to its wholly owned subidiary.[2]

Contrary to petitioners' contention (Pet. 3-5, 9), the decision below does not conflict with *Century Electric Co.* v. *Commissioner*, 15 T.C. 581 (1950), aff'd, 192 F.2d 155 (8th Cir. 1951), cert. denied, 342 U.S. 954 (1952). There, the property involved was a mixture of depreciable and nondepreciable assets (*i.e.*, a foundry in which electric motors were manufactured, a railroad siding, and the underlying land), most of which were depreciable. The taxpayer, which had previously owned the property in fee simple, sold it to an unrelated tax-exempt organization for cash in an amount less than its basis in the fee, with a leaseback for a term of 25 to 95 years. 192 F.2d at 158. The issue was whether the taxpayer's tax basis in the leasehold (*i.e.*, its basis in the fee simple interest minus the cash received) was to be depreciated over the useful lives of the assets subject to the lease rather than over the term of the lease. *Id.* at 160. The court held that taxpayer's interest was to be depreciated over the term of the lease, because the interest owned by the taxpayer was the leasehold, not the separate assets.

---

[2]Petitioners attempt (Pet. 8-9) to distinguish *Georgia R.R. & Banking* on the ground that there the taxpayer acquired its terminable interest in the stock by transferring less than the full fee simple interest to the shareholders, while here Lomas allegedly tranferred the entire fee and received in exchange all of Country Club's stock and the 40-year estate. But the transfer documents make clear that the interest which Lomas transferred to Country Club was less than the full fee simple, and that the 40-year estate was a retained interest. Just as in *Georgia R.R. & Banking*, Lomas owned the entire fee simple interest in the golf course facilities prior to the transfer. After the transfer, it had the right to beneficial use of the property for 40 years, a right which it had before the transfer. It made no investment in the 40-year estate apart from that which it made to acquire the fee simple interest.

In *Century Electric Co.*, the bulk of the property was unquestionably depreciable, there was no creation of a depreciable interest through a gratuitous division of the property rights comprising the fee simple interest between related parties, and the only issue was the time period over which the depreciation was to be taken. Furthermore, the taxpayer completely divested itself of its fee interest by transferring the property to an unrelated third party, and the leaseback interest which it obtained in (partial) consideration for the fee was truly a wasting asset.[3] See also *Miller* v. *Commissioner*, 68 T.C. 767, 775-779 (1977). None of these factors is present here.

It is therefore respectfully submitted that the petition for a writ of certiorari should be denied.

REX E. LEE
Solicitor General

MARCH 1983

---

[3]At the same time that Lomas' interest in the estate for 40 years was diminishing in value, there was a corresponding increase in the value of Country Club's remainder interest in the golf course. Since Lomas owned all of the Country Club stock, and since the value of the stock would increase as the value of Country Club's interest in the golf course increased, Lomas suffered no economic loss from the expiration of its 40-year estate. This stands in marked contrast with the situation in *Century Electric Co.*, where the taxpayer would suffer a real loss from the expiration of the leasehold estate as a consequence of the fact that an unrelated third party held the fee interest. Here petitioners simply shifted non-wasting assets from one corporate pocket to another without any overall economic loss from the use of the properties in their businesses.

DOJ-1983-03